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UNCLAS SECTION 01 OF 02 PRETORIA 004027

SIPDIS

SENSITIVE

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TAGS: ETRD ECPS EINV ECON SF
SUBJECT: HUGE TRANSNET LOSSES FORECAST SELL-OFF OF STATE ASSETS

REFTEL: A) PRETORIA 3113

B) PRETORIA 1396
C) PRETORIA 713

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¶1. (SBU) SUMMARY. Transnet's Annual Report revealed a bloated, inefficient and undisciplined state-owned enterprise (SOE) that suffered a R6.3 billion loss last year. CEO Maria Ramos plans to divest all non-core businesses and focus on providing integrated, seamless transport and logistics services. Spoornet, National Ports Authority (NPA), South Africa Port Operations (SAPO) and Petronet will remain in the Transnet fold. All other operations, including SAA, will be housed in an investment portfolio for potential future sale or disinvestment. This indicates that, despite perceptions to the contrary, and in the face of stiff opposition from labor, government has not backtracked on divestiture of non-core or non-strategic assets. In addition, Public Enterprises Minister Alec Erwin replaced the entire Board of Directors at Transnet and most of the Board at SAA. END SUMMARY.

RAMOS - A BUREAUCRATIC SUPERHERO

¶2. (U) Just eight months after taking over as CEO of Transnet, Maria Ramos has proposed major changes to improve the efficiency and profitability of the behemoth state-owned enterprise that manages the country's transport services. As the former Director General for National Treasury, Ramos established a reputation for her business-like, no-nonsense approach to government. She was instrumental in creating and implementing South Africa's sound fiscal policy resulting in lower inflation and interest rates and less government debt. In Transnet's 2003-2004 Annual Report, released August 27, Ramos paints a picture of a bloated, inefficient state-owned enterprise (SOE). Ramos said that "Transnet has shown an increasing inability to respond to the demands of its business environment" and she made it clear that a significant restructuring of Transnet resources is about to occur.

FORLORN FINANCIAL FIGURES

¶3. (U) Transnet reported a net loss of R6.3 billion for the year ended March 30, 2004 from a R421 million loss in the same period a year ago. The loss was due mainly to a R4.2 billion impairment charge, which includes a R3.5 billion write-down of aircraft and a R526 million write-down of Transnet's investment in the Second National Operator (SNO). The Transnet Group delivered revenue growth of only 5.7 percent (from R41.3 billion to R43.6 billion), well below the average annual growth of 14 percent achieved over the previous three years, and also below the 2003 inflation figure (CPIX) of 6.8 percent. Operating profit declined from R5.1 billion last year to R187 million this year. A major factor in Trasnet's dismal financial results was South African Airways (SAA) hedging loss of R8.7 billion last year. Over the past two years, SAA has reported losses totaling R15 billion. The losses result from hedges SAA made on the dollar-to-rand exchange rate after it purchased 38 new Airbus aircraft in 2002. The deal was based in U.S. dollars.

A NEW TRANSNET STRATEGY

¶4. (U) To reverse Transnet's slide into financial oblivion, Ramos unveiled a new strategy. She said that Transnet's core mission is "to provide an integrated, seamless transport and logistics solution." To accomplish this, Ramos announced that she would keep Spoornet, the NPA, SAPO, and Petronet at Transnet. All other operations, including SAA, will be housed in an

investment portfolio for potential future sale or disinvestment (Reftel A). Ramos also said that Transnet's corporate office would be drastically trimmed. The corporate office employs nearly 700 staff and incurred costs of more than R600 million last year. Transnet sources say that the corporate office staff will be reduced to about seventy people.

¶5. (U) Ramos revealed that Transnet's strategy going forward is based on the following 4-point plan: a) "redirect the business" to focus on core operations; b) "restructure the balance sheet" by eliminating outstanding debt and non-core businesses; c) "implement and adopt strict corporate governance principles" to overcome existing gaps in Trasnet's financial management processes; and 4) "adhere to a vigilant risk management process" to avoid risk-laden ventures such as SAA's hedge book. To assist in the implementation of this strategy, Ramos has earmarked R30 billion for capital investment over the next five years.

TRANSNET'S TOP PERFORMERS

¶6. (U) Among the few bright spots in the report were the NPA, with an 18 percent improvement in operating profit, SAPO, which exceeded its planned operating profit by 9 percent, and Petronet, which doubled its profit before tax to R240 million over last year. Ramos pointed out that these companies "collectively generate acceptable profitability levels," further underscoring Ramos' strategy to hold on to these operations.

BOARD OF DIRECTORS REPLACED AT TRANSNET, SAA

¶7. (U) Minister of Public Enterprises Alec Erwin also announced the replacement of the entire Board of Directors for Transnet and most of the Board at SAA. Frederik Phaswana, formerly Chairman and CEO of BP Southern Africa, takes over as Chairman of the Transnet Board. Khaya Ngqula leaves his position as President and CEO at the Industrial Development Corporation of South Africa to become the new CEO at SAA.

COMMENT

¶8. (SBU) The annual report shows government supports Ramos in her plans to reshape Transnet. It also indicates that, despite perceptions to the contrary, and in the face of stiff opposition from labor, government has not backtracked on divestiture of non-core or non-strategic assets. Public Private Partnerships, including concessions, will be a vital element of the new business model.

FRAZER